

No. 6/43/DPNP

Jakarta, October 7, 2004

CIRCULAR LETTER

To

ALL COMMERCIAL BANKS

IN INDONESIA

Concerning: Implementation of Risk Management for Banks Engaging
In Joint Marketing Efforts with Insurance Company
(*Bancassurance*)

With regard to the rapid increase in insurance companies' marketing activities conducted in partnership with Banks (*bancassurance*), it is realized that such activities bring benefits as well as potential risks to Banks especially legal risk and reputational risk. Therefore, in order to support the growth of financial market, to increase the implementation of risk management by Banks, to protect the interests of Bank customers and in accordance with the Decree of The Minister of Finance No. 426/KMK 06/2003 concerning Business Licenses and Institutional Aspects of Insurance and Reassurance Companies and to further implement Bank Indonesia Regulation No. 5/8/PBI/2003 dated 19 May 2003 concerning the Implementation of Risk Management for Commercial Banks (State Gazette of Republic Of Indonesia Year 2003 Number 56, Supplement to State Gazette of Republic of Indonesia Number 4292), it is considered necessary to regulate the implementation of risk management for Banks doing joint marketing efforts with insurance companies (*bancassurance*) as follows:

I. GENERAL

1. Joint marketing efforts between Banks and insurance companies (*bancassurance*) may be implemented by means of:
 - a. *Marketing/Distribution Agreement*, i.e. an agreement between Bank and insurance company that Bank will market insurance products to customers by face to face offering (*direct marketing*), using means of communications (*telemarketing*), or mail delivery (*direct mailing*);
 - b. *Strategic Alliance Agreement*, i.e. an agreement between Bank and insurance company to market insurance products by way of : (i) modification of insurance with Bank products to meet customers' needs or (ii) use of Bank's marketing channels including Bank's office spaces by insurance company (*channel management*);
 - c. *Joint Venture*, i.e. Bank and insurance company jointly establish a company to market insurance products;
 - d. *Financial Services Group*, i.e. a more integrated form of collaboration between Bank and insurance company, in which insurance company is allowed to establish or buy a Bank and vice versa.
2. Banks doing *bancassurance* activities should consider prevailing regulations on banking and insurance, such as Bank Indonesia Regulation No. 2/19/PBI/2000 dated 7 September 2000 concerning Prerequisites and Procedures in Giving an Order or a Written Permit to Disclose Bank's Confidentiality, Bank Indonesia Regulation No. 5/8/PBI/2003 dated 19 May 2003 concerning Implementation of Risk Management for Commercial Banks, and Decree of The Minister of Finance No. 426/KMK.06/2003 dated 30 September 2003 concerning Business License and Institutional Aspects of Insurance and Reassurance Companies.

3. While doing *bancassurance* activities, Bank is not permitted to undertake, either alone or jointly, the risks arising from insurance activities.

II. IMPLEMENTATION OF RISK MANAGEMENT

1. Bank implementing *bancassurance* activities is obligated to implement Risk Management effectively according to Bank Indonesia Regulation No. 5/8/PBI/2003 concerning Implementation of Risk Management for Commercial Banks since Bank will have to deal with various risks related to such activities, particularly Legal Risk and Reputational Risk. Implementation of such Risk Management, among others, shall cover but not limited to the following :
 - a. appointment of insurance company to become Bank's partner;
 - b. formulation of partnership agreement;
 - c. implementation of rules regarding Bank confidentiality; and
 - d. application of customer protection principles.

Implementation of Risk Management set forth in letter a to d above shall prevail for *bancassurance* activities with an insurance company which is or is not a related party of the concerned Bank.

2. In implementing Risk Management as set forth in point 1.a above, Bank is obligated to make a selection over insurance companies which will become the Bank's partner in *bancassurance* activities with attention paid to the following matters:
 - a. Insurance company eligible to become a partner is one that complies with the minimum level of solvability according to prevailing rules;

- b. Bank is obligated to ensure that partner insurance company has obtained the relevant license from The Minister of Finance to run *bancassurance* activities according to prevailing rules;
- c. Bank is obligated to monitor, analyze, and evaluate performance and or reputation of partner insurance company periodically at least once a year;
- d. Bank is obligated to end the partnership before the end of agreement period or may not extend the period of partnership if:
 - 1) performance of partner insurance company no longer meets conditions as set forth in letter a above; and or
 - 2) there has been a decrease in reputation of partner insurance company with significant influence on Bank's risk profile.
- e. In the event that the marketed insurance is linked to investment (*investment link/unit link*), Bank is obligated to ensure that partner insurance company has complied with conditions stipulated by The Minister of Finance, which, among others, are as follows:
 - 1) Availability of an expert whose qualifications equal to a deputy investment manager with at least 3 (three) years experience in his/her field;
 - 2) Separation of insurance company's assets and obligations originated from investment linked insurance from assets and obligations originated from other life insurances; and
 - 3) Implementation of other matters required in managing the investment funds entrusted by customers optimally, professionally, and independently.

3. To implement Risk Management as set forth in point 1.b above, in formulating the agreement with partner insurance company, Bank is obligated to consider the following :
 - a. Clarity of rights and obligations of each party (Bank and insurance company, including insured customer);
 - b. Each agreement should only consist of one form of cooperation as set forth in point 1.1, mentioning specifically the types of insurance marketed;
 - c. Clarity of period of agreement;
 - d. Stipulation of a clause containing the condition to revoke the partnership agreement including a clause enabling Bank to terminate partnership before the end of agreement period for reasons among others as set forth in point II 2.d;
 - e. Clarity of settlement of each party's rights and obligations (Bank and insurance company, including insured customer) should partnership agreement end.
4. In implementing Risk Management as set forth in point 1.c above, Bank is obligated to ensure that the use of customer data does not violate the regulations regarding Bank Confidentiality as set forth in Article 1 point 28 and Article 40 of Act Number 7 Year 1992 concerning Banking as amended by Act Number 10 Year 1998 and other related legislations. Actions to take, among others, are as follows:
 - a. To comply with prevailing regulations concerning Prerequisites and Procedures in Giving Orders or Written Permits to disclose Bank Confidentiality, such as based on a request, an approval or a written

- delegation of power from customer to use customer data by specifically mentioning the intention, types of desired data and insurance involved;
- b. To notify partner insurance company not to use customer data as set forth in letter a for purposes other than those approved by customer;
 - c. To require partner insurance company to keep the confidentiality of customer data as set forth in letter a even after the partnership agreement ended or has been terminated; and
 - d. Not to pass on customer data to any third parties (*outsourcing*) in the event that Bank uses third party services in the insurance marketing partnership.
5. In applying Risk Management as set forth in point 1.d above, Bank is obligated to implement basic principles of transparency related to marketed insurance such as:
- a. Explaining the following orally and in writing to customers:
 - 1) Marketed insurance product is not Bank's product and is not covered in the government guarantee program;
 - 2) Uses of logo and or other Bank's attributes in brochures or other marketing documents may not be interpreted that such insurance is Bank product;
 - 3) Characteristics of insurance such as features, conditions, risks, benefits, insurance expenses and claim procedures;
 - b. In the event that the insurance product marketed is a result of development with Bank product (*bundling product*) :
 - 1) Bank is obligated to explain to customer orally or in writing the rights and obligations of each party;

- 2) Each customer must individually receive insurance policy or evidence of participation if he/she is enrolled in a collective insurance product;
- c. In the event that the insurance product marketed is linked to investment (*investment link/unit link*) :
- 1) Bank is obligated to explain orally and in writing to the customer the characteristics of such investment, covering at least the investment asset portfolio, procedures and parties conducting the unit value valuation, investment manager, custodian bank, investment risks, prerequisites and procedures to redeem and the party responsible for delivering the report on unit value valuation to the customer;
 - 2) Bank is forbidden to warrant or participate in giving a warranty either directly or indirectly, if such investment-linked insurance offers a fixed rate of income/return.
- d. Explanation from Bank as set forth in letter a to c above should be made by a Bank officer with qualifications to comply with prevailing regulations such as:
- 1) Possession of a certificate of agency issued by a related association; and
 - 2) Having received training on the insurance product marketed.
- e. Bank is also obligated to require the insurance officers who offer insurance in bank offices (in-branch sales) to comply with the provisions set forth in letter a to c above;
- f. In the event that Bank decides to end or terminate the partnership agreement, Bank is obligated to announce such decision in writing to all customers, including the follow-up of rights and obligations settlement in connection with the insurance product marketed.

III. RISK MANAGEMENT GUIDELINES

1. Implementation of Risk Management as set forth in point II above should be stipulated into written policies and procedures in accordance to Bank Indonesia Regulation Number 5/8/PBI/2003 concerning the Implementation of Risk Management for Commercial Banks.
2. Banks which already perform *bancassurance* activities and have written policies and procedures for risk management implementation related to *bancassurance* activities but not yet complied with the provisions on implementation of risk management as set forth in point II above must adjust their policies, procedures and *bancassurance* activities not later than 6 (six) months since this regulation comes into effect.

IV. REPORTING

1. Banks implementing *bancassurance* activities for the first time are obligated to report in writing to Bank Indonesia at least 7 (seven) working days since such activities are effectively implemented according to Article 25 Bank Indonesia Regulation Number 5/8/PBI/2003 concerning the Implementation of Risk Management for Commercial Banks, using a format as set forth in Bank Indonesia Circular Letter Number 5/21/DPNP dated 29 September 2003 which contains:
 - a. Standard operating procedures (SOP) of *bancassurance*;
 - b. Organization and authority to implement *bancassurance*;
 - c. Risk identification in relation to *bancassurance*;
 - d. Test results of *Bancassurance* risk measurement and monitoring method;
 - e. Result of *bancassurance* legal aspect analysis.

2. The reporting obligation as set forth in point 1 above is exempted for Banks which had effectively implemented *bancassurance* activities before such Banks have accomplished the action plan as set forth in Bank Indonesia Regulation Number 5/8/PBI/2003 concerning the Implementation of Risk Management for Commercial Banks.
3. The report as set forth in point 1 above shall be submitted to Bank Indonesia at the following addresses :
 - a. relevant Directorate of Bank Supervision, Jl. M.H. Thamrin No. 2, Jakarta 10110, for Banks with head offices in the work area of Bank Indonesia Head Office; or
 - b. Local Bank Indonesia Regional Office, for Banks with head offices outside the work areas of Bank Indonesia Head Office.

V. MISCELLANEOUS

1. To improve effectiveness of risk management implementation, Banks performing *bancassurance* activities are obligated to conduct evaluation and audit towards such activities in compliance with risk management implementation as set forth in point II above.
2. If necessary, Bank Indonesia may conduct examination regarding the effectiveness and accuracy of risk management implementation particularly in connection with *bancassurance* activities by Banks.

VI. SANCTIONS

1. Violations of reporting obligation as set forth in point IV will be imposed with a sanction as stipulated in Article 33 of Bank Indonesia Regulation

Number 5/8/PBI/2003 concerning Implementation of Risk Management by Commercial Banks.

2. Violations of risk management implementation as set forth in point II may result in administrative sanctions as set forth in Article 34 of Bank Indonesia Regulation Number 5/8/PBI/2003 concerning Implementation of Risk Management by Commercial Banks.

VII. CLOSING

This Bank Indonesia Circular Letter shall come into effect as of 7 October 2004.

For the public to be informed, it is ordered that this Bank Indonesia Circular Letter be promulgated in the State Gazette of Republic of Indonesia.

Please be informed accordingly.

BANK INDONESIA,

MAMAN H. SOMANTRI
DEPUTY GOVERNOR